economic trends

July 2013

Households drive economic activity in first half of 2013

Albertans have sharply increased their spending on consumer products and housing so far in 2013, reflecting a strong labour market and soaring in-migration. Retail sales are up considerably over 2012 and, unlike much of the country, Alberta's housing market continues to post strong gains.

The Alberta floods caused serious damage and temporary supply disruptions in late June and into July, likely hurting economic output in the immediate aftermath. However, the movement into reconstruction should put upward pressure on certain economic indicators in the second half of 2013, such as housing starts, employment and retail spending.

Key Indicators All indicators seasonally adjusted unless otherwise indicated

Indicator	Latest Month	Value	Change year-over-year (y/y)
Employment (thousands)	June	2,201	+2.6%
Unemployment Rate	June	5.0%	+0.4 p.p.
CPI Inflation	June	2.3%	+1.0 p.p.
Retail Sales	May	$6.1B	+7.9%
Housing Starts (annualized)	June	38,141	+12.9%
Rigs Drilling (unadjusted)	July	187	-5.7%
Manufacturing Shipments	May	$6.2B	+1.5%
Exports (unadjusted)	May	$8.5B	+11.7%

Source: Statistics Canada, CAODC, CMHC. p.p.= percentage points

Alberta Household Sector

Auto sales buoy retail activity

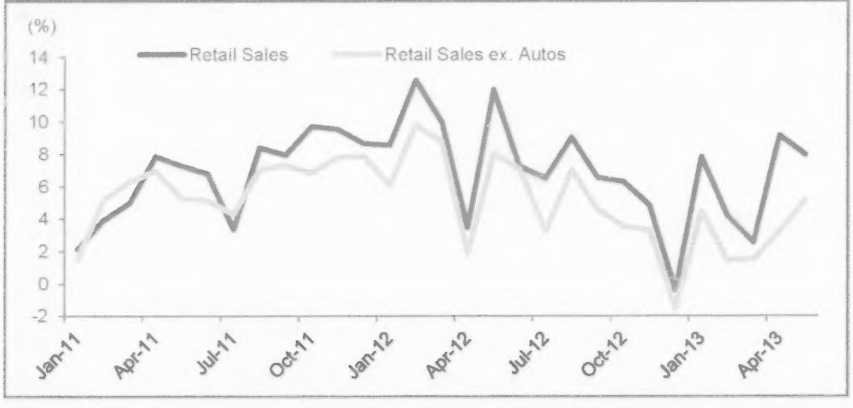
A large influx of migrants and a robust labour market has spurred retail sales in Alberta this year. Increases in April and May have pushed the province's year-to-date growth up to 6.6%, the highest among the provinces. Sales at automobile dealers continue to be the largest contributor to growth (Chart 1). The flood may add further to auto sales as damaged vehicles are replaced. Sales at grocery stores and gasoline stations are also large contributors to growth so far this year.

Solid job gain in first half; labour force swells

Alberta's rate of job creation has remained strong this year. While job growth paused in June, May and April were two of the strongest months since mid-2011. Alberta's employment in the first half of 2013 was up 2.1% compared with the first half of 2012, well above the 1.4% national gain. The increase in employment was roughly split between private and public sector jobs and entirely in full-time positions.

Strong migration to Alberta has led to more people entering the labour market in search of work. Therefore, despite solid job growth, the unemployment rate has inched higher in recent months. In June, the unemployment rate rose to 5.0%, its highest level since January 2012, but still well below the national average of 7.1%.

Chart 1: Alberta Retail Sales (year-over-year growth)



Source: Statistics Canada

Calgary leads new housing price gains, Edmonton leads in housing starts

After several years of fairly flat or negative growth, Alberta's new housing price index has been accelerating since early 2012. In May, the index rose 2.7% year-over-year, the highest growth since April 2008. Among the major centres, Calgary is leading these gains, up 5.3% compared with almost no change in Edmonton. However, Edmonton is leading the two cities in new home construction. In the first half, Edmonton housing starts were up 67% over the first half of 2012, whereas Calgary posted a 24% decline.

In the resale market, Alberta moved firmly into seller's market position with a sales-to-new listing ratio of 0.64 in June. This reflects an increase in sales and a pullback in listings. The June estimates were likely impacted by the flooding in southern Alberta, which contributed to a drop in new listings in Calgary. The flood is expected to put upward pressure on residential building activity in the coming months as reconstruction ramps up.

Earnings and price growth accelerate

Earnings growth in Alberta has shown persistent strength, largely due to increases in hourly wages. In the first five months of 2013, average weekly earnings are up 3.9% over the same period last year, well above the 2.3% national gain.

Alberta's consumer price inflation rate rose above 2.0% during the last two months, propped up by higher prices for vehicles, gasoline and housing. After twelve months of subdued inflation, ranging between -0.5% and 1.4%, inflation has returned closer to its historical average.

Alberta Business Sector

Non-residential construction spending levels off

After a strong start to the year, spending on non-residential construction investment dipped slightly in the second quarter of 2013. This bucks an otherwise upward trend that has been observed since late 2011. Year-to-date growth eased to 1.9%, weighed down by a decline in the commercial sector. At the city level, there have been mixed results, with Calgary's spending up 3.4% year-to-date, but Edmonton's down 4.0%. Moving forward, strong non-residential building permits (up 22.0% year-to-date as of May) and flood-related reconstruction will likely add to construction activity later this year.

Manufacturing output slow to recover from late 2012 drop

Alberta shipments of manufactured products have stayed within a fairly narrow band since mid-2012; however, May saw the first year-over-year increase in eight months, lifted by a jump in chemical shipments. Recent manufacturing sales have been weighed down by a temporary refinery shutdown. Should current trends continue, shipments are likely to come in above last year's levels in the second half of 2013, reflecting a slump in shipments in the latter part of 2012.

Exports jump on higher energy product shipments

In May, Alberta saw its largest year-over-year export increase (+11.7%) in over a year, propelled by a higher value of energy product shipments. Base period effects, namely the weakness in exports in the second half of 2012 (see Chart 2), coupled with the recent increase in oil prices, will put upward pressure on year-over-year growth rates in the coming months.

Year to date, international exports are up by 3.0% over the same time last year. Chemical, plastics and rubber products - Alberta's largest export category outside of energy products - has had a particularly strong start to the year (+14.3% year-to-date).

Global Economy

IMF downgrades global economic growth again

The International Monetary Fund (IMF) downgraded its forecast for global growth for the fifth consecutive time in the July update to its World Economic Outlook. World output growth was revised down by 0.2 percentage points in both 2013 and 2014 to 3.1% and 3.8% respectively. The IMF again advocated for greater financial integration in Europe, as well as detailed medium-term public debt reduction policies that take into account the need for near-term growth.

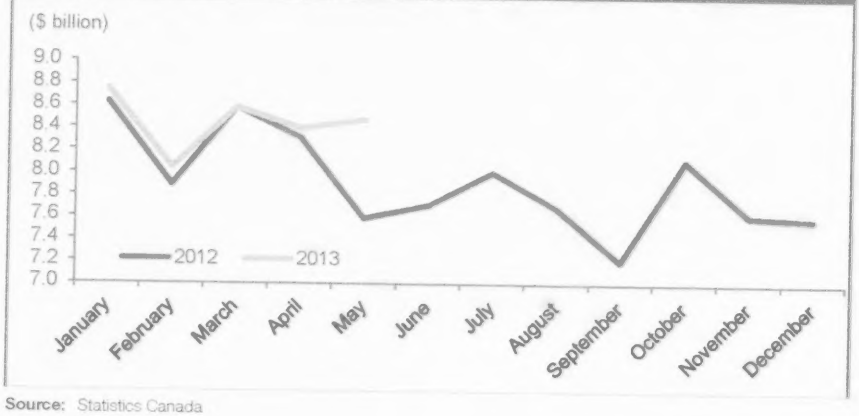
Uneven economic growth expected by the Bank of Canada

The Bank of Canada expects Canadian real GDP growth to be "choppy" in 2013 before gaining momentum in 2014. The Bank attributes the choppiness in part to the flooding in southern Alberta. They estimate that disruptions from the flood will subtract 0.7 percentage points (annualized) from Canadian real GDP growth in the second quarter, while reconstruction efforts will add 1.0 percentage points to third quarter growth. The Bank expects real GDP to grow by 1.8% in 2013, roughly in line with the 2012 increase and similar to the IMF's latest outlook.

Divergence in US and Canadian housing

Housing markets in the US and Canada have been moving in opposite directions. In the US, year-over-year growth in both housing starts and prices have increased for much of the last two years. The opposite is true for Canada. Housing starts in 2013 are down over 2012, and year-over-year house price growth has been falling since November 2011. These diverging trends are due, in part, to the US housing market recovering from depressed levels and the Canadian market cooling after displaying symptoms of overheating in some cities.

Chart 2: Alberta International Goods Exports



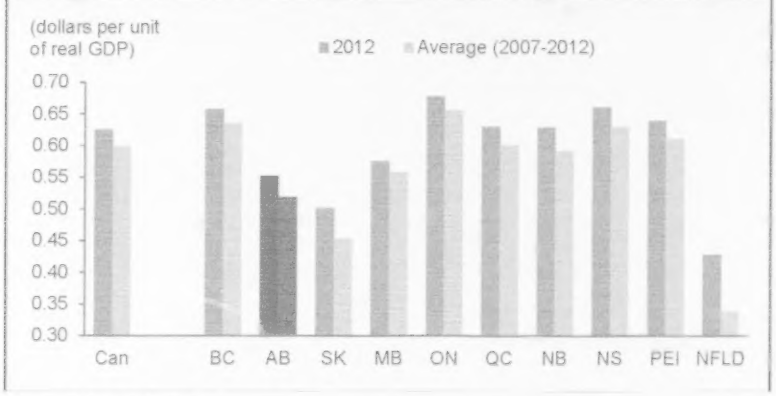
Source: Statistics Canada

How Cost Competitive is Alberta's Labour Market?

Workers in Alberta have earned the highest average wages and salaries among the provinces since mid-2005. Alberta's relatively high cost of labour, however, should not be interpreted as a sign that its workforce is less cost competitive. Focusing solely on the costs ignores how effective labour is at generating output. Alberta has one of the most productive workforces in Canada: for every hour worked, workers in Alberta generate a relatively high level of output.

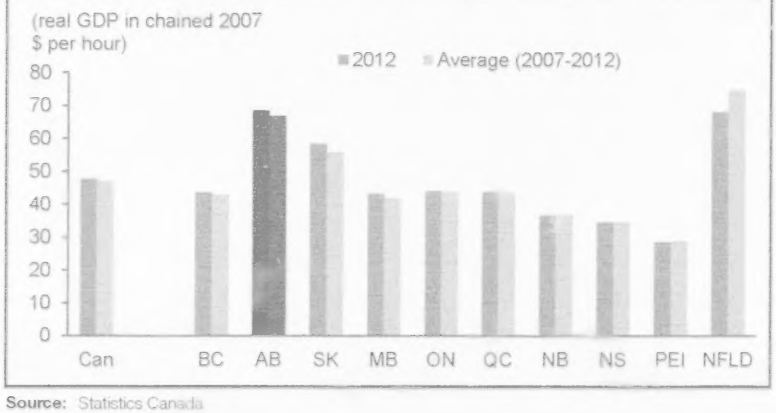
The measure that provides a more complete picture of labour cost competitiveness is known as unit labour cost (ULC), since it takes into account both labour costs and labour productivity (see blue box for definition). Based on this measure, the data indicate that Alberta's workforce is cost competitive relative to the other provinces. That is, to generate a given level of output, labour costs in Alberta are relatively low. This InFocus takes a closer look at Alberta's ULC profile and examines some of the reasons behind the province's stronger performance in this area.

Chart 1: Unit Labour Cost, Business Sector



Source: Statistics Canada

Chart 2: Labour Productivity, Business Sector



Source: Statistics Canada

Overall unit labour cost in Alberta among lowest in Canada

In spite of the generally higher average wages and salaries in Alberta, the province's overall ULC was the third-lowest among the provinces over the past five years, behind only Newfoundland and Labrador, and Saskatchewan (Chart 1). ULCs were brought down in Alberta entirely because of relatively high levels of labour productivity during that time (Chart 2). Newfoundland and Labrador, and Saskatchewan also posted high productivity levels; similar to Alberta, these two provinces are noted for their active mining, oil and

Calculating unit labour cost

Unit labour cost is frequently used to measure labour cost competitiveness and long-term inflation pressures stemming from labour income increases. Based on data from Statistics Canada's Productivity Accounts, unit labour cost can be calculated by dividing labour compensation per hour worked by labour productivity:

$$\text{Unit Labour Cost} = \frac{\text{compensation / hour}}{\text{real GDP / hour}}$$

Labour compensation represents all payments in cash or in kind earned by workers, including employers' social contributions (e.g., health benefit plans) and estimated labour income for self-employed workers.

Labour productivity is real gross domestic product (GDP) per hour worked.

If labour compensation rises faster than increases in labour productivity, unit labour cost will increase, correspondingly.

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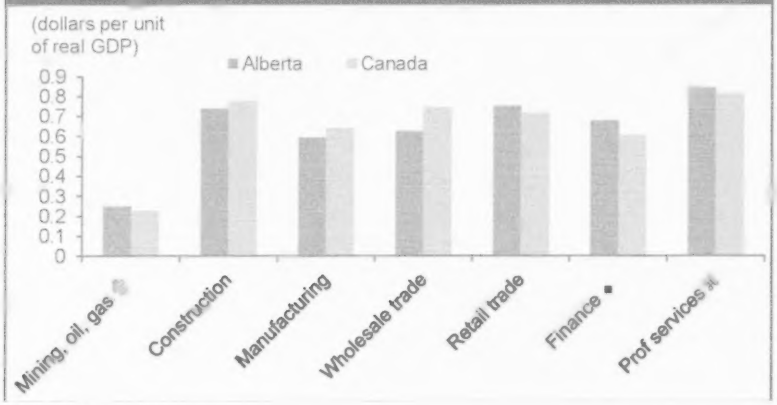
gas sectors. Looking at Charts 1 and 2 together, productivity can have a strong offsetting effect on labour costs, thereby improving an economy's labour cost competitiveness.

Alberta's ULC lower than national average in some industries, higher in others

An investigation of ULC by industry reveals two things. First, ULCs vary significantly by industry in Alberta and for Canada as a whole, with mining and oil and gas extraction posting one of the lowest readings (Chart 3). This industry has low ULCs because its labour productivity is usually the highest among the industries, a reflection of its high capital intensity. A high level of productivity has more than offset the elevated wages and salaries found in this sector. In contrast, manufacturing's ULCs are typically at least twice as high as those for mining and oil and gas extraction.

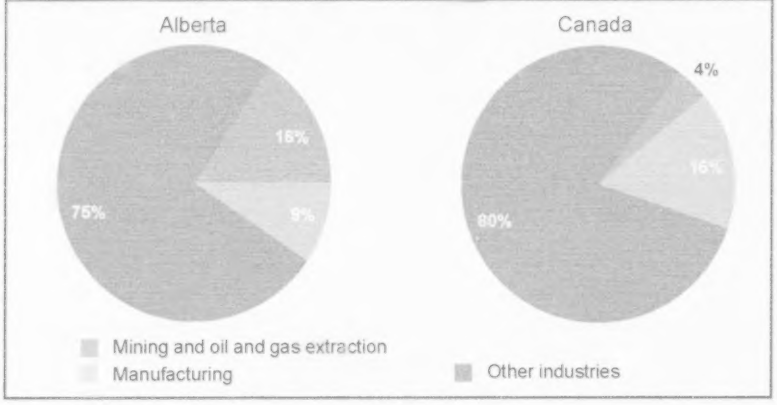
Second, Alberta is more labour cost competitive than the national average in some key industries such as manufacturing, construction and wholesale trade (Chart 3); however, Alberta lags behind the national average in other major industries, including mining and oil and gas extraction, retail trade, and professional, scientific and technical services. The mixed results indicate that Alberta's relatively low overall ULC is not a result of greater labour cost competitiveness across all industries.

Chart 3: Average Unit Labour Cost by Industry (2007-2012)



Source: Statistics Canada.
* Mining and oil and gas extraction
◆ Finance and insurance, and holding companies
⌘ Professional, scientific and technical services

Chart 4: Average Share of Total Labour Compensation (2007-2012)



Source: Statistics Canada.

Industrial composition plays a pivotal role

Industry composition helps explain why Alberta's ULCs are lower than the national average. Chart 4 shows that Alberta has a relatively high share of labour compensation in one of the lowest ULC industries: mining and oil and gas extraction. This industry accounted for 16 per cent of total labour compensation, compared with the national average of 4 per cent. At the same time, manufacturing's share in Alberta was only 9 per cent, well below the national average of 16 per cent.

Mining and oil and gas extraction's significantly lower ULC, combined with its considerably larger weight relative to manufacturing, is a key reason for the province's relatively low overall ULC. Similar findings were also revealed for Saskatchewan and Newfoundland and Labrador, the latter of which achieved exceptionally high labour productivity levels for its mining and oil and gas extraction industry.

Conclusion

Despite having the highest average wages and salaries among the provinces for several years, Alberta's workforce appears to be more labour cost competitive than the national average overall once labour productivity is taken into account. Alberta's unit labour costs are the third-lowest among the provinces, in large part due to the fact that the mining and oil and gas extraction industry has a relatively low unit labour cost and accounts for a significantly larger share of labour income compared with the rest of the country.

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